Financial Rights
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FACT SHEET

CALL THE CREDIT & DEBT HOTLINE ON
1800 007 007

Financial Rights Legal Centre
ABN 40 506 635 273

Fact sheets are information only and should not be relied upon as legal advice. This information only applies to NSW.

DEBT AGREEMENTS

This fact sheet is for information only. It is recommended that you get legal advice about your situation.

WARNING: DEBT AGREEMENTS ARE AN ACT OF BANKRUPTCY AND MAY SERIOUSLY AFFECT YOUR CREDIT REPORT. ALWAYS GET INDEPENDENT ADVICE FROM A FREE FINANCIAL COUNSELLOR BEFORE ENTERING INTO A DEBT AGREEMENT BY CALLING 1800 007 007. DEBT AGREEMENTS ARE ONLY ONE OPTION FOR CONSUMERS TO CONSIDER WHEN HAVING TROUBLE PAYING DEBTS. GET ADVICE ON THE BEST OPTION FOR YOU IN YOUR CIRCUMSTANCES.

CASE STUDY

Rushika was struggling with repayments on 3 credit cards and a personal loan. She works but she is a very junior employee and never seems to be able to pay much more than the interest on her credit cards. She came across an advertisement on the internet for a service called Beat Debt Solutions which promised to stop the interest on her debts and wrap all her debt repayments up into one easy payment.

She called the service and ultimately signed up for a Debt Agreement. At first it seemed like a great deal but then she found she had difficulty getting a pay TV service for the flat she was renting because the Debt Agreement was on her credit report. Next she had to move because her landlord wanted to sell her flat and she took ages to find a new place to rent because she kept being knocked back.

Two years later she lost her job and had to apply to vary her payments on the Debt Agreement. The Debt Agreement was originally meant to be 4 years long and the variation took it out to 5 years. She had only had two years to go on her personal loan when she first signed up. Six months later she fell pregnant and could not pay at all. After another 6 months the Debt Agreement was terminated and all her creditors are chasing the debts again plus back interest. Because a significant proportion of her repayments went to cover the costs of administering the agreement, she is in a worse position than ever!

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Financial Rights
LEGAL CENTRE

FACT SHEET

WHAT IS A DEBT AGREEMENT?

Debt Agreements are a formal alternative to bankruptcy under the Bankruptcy Act for people who are insolvent (unable to pay their debts as they fall due). Under a Debt Agreement your creditors (people and organisations you owe money to) agree to accept less than the full amount of the debts owing in return for a commitment by you to meet regular repayments for an agreed period of time. A person or organisation called a Debt Agreement Administrator would help you to propose the agreement and then takes your repayments to distribute to your creditors. Some of each repayment is kept by the Debt Agreement Administrator for administering the agreement.

If you make all the repayments under the agreement, you are then released from the remainder of the debts included in the agreement. If you fail to make it to the end of the agreement (you do not make all the repayments) then the deal is off and the creditors will go back to chasing the whole debt, plus any interest that has accrued in the meantime.

Unlike going bankrupt, you may keep your assets, such as a home you are paying off, but there are many other consequences that are very similar to bankruptcy (like the Debt Agreement being listed on the National Personal Insolvency Index [NPII] and your Credit Report).

Debt Agreements are heavily promoted by private firms who set up and/or administer Debt Agreements for a fee and the number of Debt Agreements has grown considerably in recent years. Debt Agreements are often marketed as a type of interest free "loan consolidation" when this is misleading. It is important to understand the risks and consequences of entering a Debt Agreement and what your other alternatives might be.

Debt agreements are regulated by the Australian Financial Security Authority (formerly the Insolvency Trustee Service of Australia) known as "AFSA". There is more information about Debt Agreements, Bankruptcy and Personal Insolvency Agreements on the AFSA website at www.afsa.gov.au.

A FREE ALTERNATIVE: AGREEMENTS WITH YOUR CREDITORS THAT DO NOT INVOLVE BANKRUPTCY LAW

If you are genuinely unable to pay your debts as they fall due, you may be able to come to an agreement with your creditors to pay a reduced amount, postpone some repayments, reduce the interest rate and/or reduce your repayments. If you are in financial hardship and cannot repay your loans (including credit cards) you may also have rights under the National Credit Code: See Fact Sheet: Hardship variations on consumer loans.

An arrangement like this has all the advantages of a Debt Agreement, without the need to pay an administrator. An agreement such as a hardship variation may affect your ability to get more credit from your existing credit providers, at least in the short term, but it should not affect your credit report unless you have already defaulted before you make an arrangement (the default will remain listed for 5 years). A hardship variation or other arrangement with your creditors will not appear on the NPII.

KEEP PAYING

Sometimes debtors are encouraged to enter Debt Agreements to reduce their interest or simplify their repayments but they are not really insolvent. If you can actually meet your repayments without real hardship a Debt Agreement is not really appropriate because it will damage your ability to get credit and other services in the future. You may be able to refinance to a lower interest rate and/or consolidate your debts to make things easier. You may have options for increasing your income or reducing your expenditure. See Money Smart at www.moneysmart.gov.au for options

Warning: Do not refinance to a loan with a higher interest rate in order to consolidate your debts. If you refinance credit card debt, be careful not to run up further credit card debt afterwards – cut up the card(s) until you have paid off the consolidated debt.

CONSIDER BANKRUPTCY (FILING A DEBTOR'S PETITION)

If you are really in financial hardship (you cannot afford your loan repayments and your essential living expenses) you may wish to consider Bankruptcy, particularly if you do not own any assets (real estate, shares etc) that would be taken and sold in Bankruptcy.

Bankruptcy usually last only 3 years (although it can be extended to 5 or 8 years in some circumstances) and you will only have to make income contributions (payments towards your debts) if you earn over a certain threshold amount (see www.afsa.gov.au and select current amounts).

Importantly, there is no risk that you will not be able to make your repayments and end up back where you started.

A Debt Agreement is unlikely to be your best option if all the following apply:

- You have no assets (apart from a car worth less than $7,600)
- You earn a low income
- You do not want to be a company director.
- Bankruptcy will not affect your employment

See Fact Sheet: Should I consider Bankruptcy for more information in relation to Bankruptcy

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Warning: Always consult a financial counsellor before entering Bankruptcy as there are serious consequences which you must understand, including that any money or property you receive (inherit or win for example) while you are Bankrupt will be taken to pay your debts. A financial counsellor may also be able to assist you to negotiate an informal agreement and avoid Bankruptcy or a Debt Agreement!

WHO CAN ENTER A DEBT AGREEMENT?

To be able to enter a Debt Agreement you must:

- Be insolvent (unable to pay your debts as and when they fall due); and
- In the past 10 years not have been bankrupt, entered a Debt Agreement, or given an authority under Part X of the Bankruptcy Act; and
- Have total unsecured debts of less than $108,162.60 (as at September 2015) Unsecured means that there is no mortgage over your goods or home for a loan. For example a car loan would usually be excluded from a Debt Agreement as the car can be taken if you do not pay the loan; and
- Have after tax income of less than $81,121.95 (as at September 2015); and
- Have property of value less than $108, 162.60 (as at September 2015). As a guide, property includes anything you own except household furniture, tools of trade, and a car worth less than $7,600..

THE CONSEQUENCES OF A DEBT AGREEMENT

The consequences of entering a Debt Agreement include:

- The debtor is not bankrupt (although proposing a Debt Agreement is an “act of bankruptcy” and your creditors could use it to make you Bankrupt if the Debt Agreement is not accepted or is later terminated);
- All unsecured creditors are bound by the Debt Agreement and are paid in proportion to their debts;
- You are released from most unsecured debts when you finish making your payments;
- Your name will appear on the National Personal Insolvency Index (NPII) for at least 5 years from the date the Debt Agreement was made. If your agreement is terminated before you complete it, it will be on the NPII for 5 years from when it was made or 2 years from the date it was terminated whichever is later. For example,

Financial Rights
LEGAL CENTRE

FACT SHEET

if your Debt Agreement is terminated after 4 years then the NPII listing will not be removed for 6 years from when it started. If the Debt Agreement is completed after 5 years, the listing will be removed when it is completed. If the Debt agreement was rejected or withdrawn it will be removed from the NPII after 12 months.

- The Debt Agreement is listed on your credit report for 5 years, two years from termination or until the Debt Agreement is completed – whichever is the longer);
- Secured creditors may still seize and sell any assets (e.g. a house) which you have offered as security for credit if you default in making repayments;
- Unsecured creditors cannot take any action against you or your property to collect their debts;
- Interest stops running on your unsecured debts, but only if you meet the repayments on time and successfully complete the agreement. You need to compare the benefit of no interest against the administration fees you have to pay (see below).
- Some professions or licensed trades may prevent you from continuing in your employment or require you to show cause why you should be allowed to continue in your employment
- You cannot borrow, or obtain goods and services on credit, for above a certain amount without declaring that you are in a Debt Agreement.

If you do not complete the agreement by making all the repayments you will not be released from your debts or the interest owing.

WHO MIGHT BENEFIT FROM A DEBT AGREEMENT?

If you are **insolvent** and in one of the following categories you might benefit from a Debt Agreement:

- You are paying off your home or you have other assets that would be available to your creditors in bankruptcy
- You are a company director (or about to become one). You can be a company director while you are in a Debt Agreement but not while your are bankrupt or in a Personal Insolvency Agreement.

If the above circumstances do not apply to you, a Debt Agreement will usually be unsuitable and you should investigate other options.

In either case try to make informal arrangements with your creditors first and make sure you understand the consequences of entering a Debt Agreement and the risks of not completing it. You should also note that you will have trouble refinancing a secured loan, such as a home loan, once you are in a Debt Agreement. Always get advice from an independent Financial Counsellor first.

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Financial Rights
LEGAL CENTRE

FACT SHEET

CASE STUDY

Ted & Josie are married with four children. Ted works as a storeman and earns $25,000 p.a. Josie was working as an administration officer but that job ended a few months ago. Since then it has been impossible for Ted & Josie to keep up with their loan repayments. Ted & Josie feel that they are just slipping further and further behind and will never catch up. Ted & Josie are considering going bankrupt. Then they see an advertisement saying: "Are you having trouble paying your debts – there is a way you can get released without going bankrupt! Call now."

Josie rings and makes an appointment for herself and Ted. At the meeting, the consultant tells them they meet the criteria to get a Debt Agreement. They are given a handout on Debt Agreements and told to read it. If they want to go ahead the cost is $1500 up front. Ted and Josie both say they don't have a $1500. The consultant says don't worry just stop making the loan repayments and pay the fee in instalments. Ted & Josie do this and then get a letter stating that their creditors have rejected the Debt Agreement twice and the Debt Agreement cannot go ahead. Now Ted & Josie are further behind in their loan repayments and feel they have no choice but to go Bankrupt.

FEES

Debt Agreements can be quite expensive. Administrators charge fees upfront to prepare the proposal for a Debt Agreement and fees to administer the Debt Agreement if it is accepted. So it may be better to negotiate a repayment arrangement directly with you creditors rather than pay fees to an administrator.

The upfront fees charged by administrators can vary enormously (from around $200 to over $2,000!). So shop around! A list of administrators can be obtained by phoning AFSA.

The Administrator also charges a fee for administering the Debt Agreement which includes:

a. receiving your payments and distributing this money to creditors; and

b. all the required paperwork.

DO NOT STOP MAKING PAYMENTS TO YOUR CREDITORS TO PAY FOR A DEBT AGREEMENT PROPOSAL. It is quite common for debtors to be told to stop paying their creditors and make payments towards the

Financial Rights LEGAL CENTRE

FACT SHEET

upfront fee instead. Remember that there is no guarantee your creditors will say yes to the Debt Agreement proposal and if you stop paying you will be in a worse position. You will not usually be offered a refund of the amounts paid in the event the proposal is rejected.

If you feel you have been misled or treated unfairly by a Debt Agreement Administrator (or another organisation that has taken a fee from you to refer you to a Debt Agreement Administrator), ring 1800 007 007 for legal advice.

HOW IS A DEBT AGREEMENT ARRANGED?

STEP 1: INFORMATION

You will be told why a Debt Agreement will benefit you. You will be asked to agree to paying an upfront fee (either in writing or over the phone or internet).

You should be given a Prescribed Information sheet to read about the alternatives and consequences of bankruptcy and Debt Agreements. This may not happen until you have agreed to pay a fee and spent considerable time and energy providing information about your personal details and debts. This information is available free from AFSA (www.afsa.gov.au) and you should find out what you can before agreeing to sign or pay anything.

Sometimes the person who is promoting the Debt Agreement will not be a Debt Agreement Administrator but another person who acts as a broker. This person will usually receive a fee from your or from part of what you pay the Debt Agreement Administrator. Be particularly wary of these people as they are not regulated by AFSA.

STEP 2: THE PROPOSAL IS LODGED

You complete and lodge three forms with AFSA: a Debt Agreement proposal, an Explanatory Statement and a Statement of Affairs. They must be received by AFSA within 14 days of being signed.

AFSA checks that

- you are eligible to lodge a Debt Agreement proposal;
- the Debt Agreement Administrator is eligible to administer Debt Agreements;
- the Debt Agreement Administrator has signed a certificate to the effect that the proposed agreement is affordable and sustainable; and
- all of the questions on each of the three forms is answered.

AFSA may call you to verify the information on the form or clear up any inconsistencies or concerns they may have.

Financial Rights LEGAL CENTRE

FACT SHEET

STEP 3: PROPOSAL IS SENT TO CREDITORS TO ASSESS AND VOTE ON

AFSA sends the proposal and Explanatory Statement to your creditors, asking them to detail their debts and to vote on the proposal.

Creditors assess the proposal and vote. Any questions are referred to the Debt Agreement Administrator.

A secured creditor (e.g. a car or home loan) is entitled to vote and receive dividends on the unsecured part of their debt (e.g. if you owe more on your car or home loan than the car or house is worth).

During the voting period creditors cannot demand payment of the debt against you or your property but can commence or continue legal action to get a judgment. The judgment cannot be enforced without the leave of the Court.

STEP 4: AFSA CHECKS AND COUNTS THE VOTES

For a proposal to be accepted, AFSA must receive 'yes' votes from a majority of your creditors who are owed at least 50% of your total debt between them. Even creditors who vote against the Debt Agreement are bound by it, provided the required majority have voted 'yes'.

If the proposal is accepted by the creditors, the Debt Agreement Administrator is responsible for:

- Collecting payments from the debtor;
- Keeping creditors and debtors informed;
- Paying dividends to creditors;
- Telling AFSA when the Debt Agreement is completed (or when a 3 month or 6 month default occurs).

If the proposal is not accepted by the creditors:

- It remains on the NPII and on the records of credit reference agencies;
- Creditors are able to commence recovery action including further interest accrued, since repayments were last made (that includes the period while the Debt Agreement was being prepared and considered);
- Creditors can issue a Creditor's Petition to make you bankrupt on the basis that your Debt Agreement proposal constitutes an "act of bankruptcy".

Financial Rights
LEGAL CENTRE

FACT SHEET

WHAT IF I WANT TO GET OUT OF OR CHANGE A DEBT AGREEMENT?

You can change or end a Debt Agreement if the majority in value of your creditors agree to this. You can also get out of a Debt Agreement by defaulting on the payments (see below). It is also possible to obtain a court order to get out of the Debt Agreement but you should seek legal advice before considering this option.

WHAT IF I DEFAULT ON A DEBT AGREEMENT?

The Debt Agreement is automatically terminated if:

- You have arrears which have not been repaid within 6 months;
- You do not complete making your payments within 6 months of the completion date of the agreement.

The effects of terminating a Debt Agreement include:

- Creditors can commence or recommence recovery action against you for the whole amount owed;
- The termination of the Debt Agreement is registered on the NPII
- The termination can be used as the basis for making you Bankrupt using a Creditor's Petition.

IMPORTANT NOTE: DO NOT ENTER A DEBT AGREEMENT IF YOU ARE SOLVENT (ABLE TO PAY YOUR DEBTS). DEBT AGREEMENTS HAVE SERIOUS CONSEQUENCES FOR YOUR CREDIT RATING AND ARE NOT AN EASY WAY OUT OF DEBT.

COMPLAINTS

If you are unhappy with the conduct of someone who has tried to arrange a Debt Agreement for you, or is administering your Debt Agreement you can complain.

Some examples of unsatisfactory or inappropriate conduct include:

- If your Debt Agreement Administrator demands that you pay the fees for the ongoing administration of the Debt Agreement before it has been accepted by your creditors (but they can charge a set up fee even if the proposal is not accepted);
- If your Debt Agreement Administrator (or another person/ organisation) has told you misleading information about entering a Debt Agreement.
- If your Debt Agreement Administrator fails to properly manage you debt agreement;

Financial Rights LEGAL CENTRE

FACT SHEET

- If your Debt Agreement Administrator proposed, or encourages you to propose, a Debt Agreement that you clearly cannot afford;
- If your Debt Agreement Administrator encouraged you not to fully disclose your financial position;
- If your Debt Agreement Administrator is not dealing with your inquiries or does not respond to any disputes you have raised; or
- If your Debt Agreement administrator engages in illegal conduct.

If you feel that your Debt Agreement Administrator has acted inappropriately, you should complain to your administrator first. If they do not respond satisfactorily to your complaint, you should make a complaint to 'Bankruptcy Regulation' at Australian Financial Security Australia (AFSA). The AFSA website (www.afsa.gov.au) contains contact details of how to make a complaint.

If your complaint is about a person or organisation that is not a regulated Debt Agreement Administrator regulated by AFSA, you should complain to ASIC at www.asic.gov.au.

This is only a brief guide and it is recommended that you speak to a financial counsellor to discuss the best option for you in your circumstances. See Fact Sheet: Getting Help for a list of additional resources.

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